STAKEHOLDER COMMENTS REGARDING
DRAFT JANUARY 2021 PROPOSED METRO DISTRICT CHANGES

STAKEHOLDER COMMENTS RECEIVED JANUARY 25, 2021

A. Comments on Public Improvements Cost Exhibit Requirement

A.1: Request to allow an administrative method to approve an update to the Engineer's Estimate or Probable Costs Exhibit in Service Plan instead of a formal service plan amendment approved by Council (ie City Manager approval) to address possible future contingencies that may come up.

A.2: Requiring public improvements and cost estimates as an exhibit to the service plan is common, however, we recommend that language be added to the body of the service plan that acknowledges that the public improvements and costs *are projections*. Similar to the financial plan, a district needs flexibility in its ability to respond to market demands, development changes, construction cost increases, etc. We suggest revising the definition of "Public Improvements" in Article II to add the following:

> "All descriptions of the public improvements to be constructed, and their related costs, are estimates only and are subject to modification as engineering, development plans, economics, the City's requirements, and construction scheduling may require. In addition, these initial cost estimates only include the public improvement portion of the costs and the total project improvement costs (including items such as dry utilities, etc.) will be significantly higher and will materially increase the overall costs. Upon approval of this Service Plan, the District will continue to develop and refine cost estimates contained herein and prepare for issuance of debt."

B. Comments on "Resident" and "Residential Districts" Definitions

B.1: Add "[any person who] **lives**" to definition of Resident as there may be situations in which someone lives there but doesn't own or rent (ie a kid living in a home owned by parents for which s/he doesn't pay rent).

B.2: Consider replacing "developed property" with "a developed residential lot other than a model home"

Developed property can be reasonably interpreted to include anybody who owns a landscaped parcel of open space or owns a partial interest in a model home. These are two popular types of real property assets that developers and builders rely on to qualify themselves to serve on metro district boards.

B.3: As drafted, if there is a single tax parcel assessed residential within a large, functionally commercial district, that single tax parcel would subject the district to all limitations in the service plan applicable to "Residential Districts" (i.e., mill levy caps).

C. Comments on Community Engagement Requirement (Service Plan §V.A.26)

C.1: Regarding requirement to provide written notification to residents on how to access virtual Board meeting, reads as though a post card notice has to be mailed to all residents which is very costly. Perhaps clarify that posting of such information on the District's website meets this requirement.

C.2: Section V.A.26.b does not specify a time frame to provide written information for virtual meetings nor where such information should be posted. Additionally, providing written notice of meetings will create an additional administrative expense for special districts that already have limited budgets. Since the City is implementing a website requirement it would be more efficient and cost effective to require all special districts to post notice on that website.

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D. Comments on Service Plan Amendment Requirements (Service Plan §V.A.27)

D.1: Add "minor or" before technical to tie with language in previous sentence:

"Changes to the Service Plan of a minor technical nature may be approved administratively by the City. The City shall determine if a change is **minor or** technical in nature."

E. Comments on Definition of Debt

E.1: The proposed "Debt" definition will include bonds that are issued to repay developer advances. As such, please note that the size of the debt limit will need to account for this.

E.2: The revised definition of "Bond, Bonds or Debt" states: "Bond, Bonds or Debt: means any bond, note debenture, **contract** or any other financial obligation of the District, the proceeds of which are or will be used to fund Public Improvements, and which is payable in whole or in part from, or which constitutes a lien or encumbrance on, the proceeds of ad valorem property tax imposed by the District or any other lawful revenue or funds of the District." (emphasis added).

Developer advance contracts (i.e., Operations and Capital Funding Agreements) are annual appropriation promises. As such, they do not meet the threshold of "Debt" as they are not multiple fiscal year obligations. We would appreciate the opportunity to discuss this item in more detail at the stakeholder meeting to determine the concerns the City is hoping to resolve with the addition of this language to the definition.

E.3: "Debt" now includes any bond, note debenture, contract, or any other financial obligation of the district "used to fund Public Improvements" and which is payable from, or which constitutes a lien on, ad valorem taxes or other legally available revenue of the district (Section II)

- The expansion of this definition will have the practical result of applicants requesting higher debt limitations under the service plan.

F. Comments on Interest Rates (Service Plan §VI.B)

F.1: Section VI.B. of the proposed Model Service Plan states: "Interest on any Debt of the District, or other District obligations payable in whole or in part from revenues derived from the Debt Service Mill Levy, shall be simple per annum interest and shall not compound."

It is extremely important to make a distinction between Debt issued to developers ("Developer Placed Debt") as opposed to Debt issued to the market or sold to a third-party purchaser ("Publicly Placed Debt"). If the City's objective is to assure that a community accomplish the financing for the finite public improvements with the lowest interest costs and least restrictive terms, that objective can be met by limiting Developer Placed Debt to accrue only simple interest and by allowing Publicly Placed Debt to accrue compounding interest.

A more detailed explanation of this topic is being provided by underwriters in our community.

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F.2: Regarding requirement for simple per annum interest, this change to the Model Service Plan would represent a significant deviation from what has become the standard in the state for Metropolitan District financings. It would also significantly limit early-stage borrowing options for districts as well as increase borrowing costs to those districts that could borrow in compliance with this clause.

The underlying challenge that a provision like this presents is that it eliminates an investor's ability to maintain its rate of return at the rate on the bonds if the issuer falls behind on debt service. For instance, if debt carries a 4% stated interest rate, but the issuer falls behind on payments (and then ultimately catches up), without compounding, the investor would face an ultimate rate of return on that investment that can be well below the 4% rate on the debt. This is because when issuers get behind on payments, principal is outstanding for a longer period of time, but with simple interest, the same amount of interest is received in total. Compound interest would pay interest on the unpaid interest, bringing the total return back up to the stated rate on the debt.

This is generally not a significant issue for investment grade borrowers, which encompasses the majority of municipal issuers in the country. However, in Colorado, where Metropolitan Districts frequently are used as a tool to build public infrastructure ahead of development and are not initially investment grade rated, it can be a significant factor. For early stage Metropolitan District debt, we would certainly see an increase in the interest rate the investors would require on simple interest debt in order to take the risk that if the bonds are not paid current, their return would suffer. We have seen very few issuances of this type to date, so it is difficult to accurately measure how much this penalty would cost taxpayers, but there would certainly be a premium.

Additionally, some districts need to use structures other than current interest bonds to borrow when infrastructure is needed. Convertible Capital Appreciation Bond are one such approach where interest accrues and compounds on the initially borrowed amount until the bonds convert to current interest bonds at a date in the future when the district is projected to be able to afford those payments. We have not seen an issuance like this marketed without compound interest and believe that it would be highly challenging and would require significantly higher interest rates to do so if simple interest were mandated.

None of this is to say that bonds placed with developers must have interest that compounds. Simple interest bonds to developers, while not necessarily desirable, does not pose the significant issues that it does for bonds sold to third party investors and we don't have objections to that change.

In summary, The City of Thornton would put itself in the company of a very small number of municipalities that require simple interest on bonds sold to the marketplace if this change is made. This would impact the use of the Metropolitan District tool as an early stage financing mechanism and may slow development within the City because of the widespread use of the tool. We would caution the City to consider additional input from the development and finance community before proceeding with this change.

F.3: Maximum net interest rate on Debt or other obligations payable in whole or in part from the Debt mill levy is not to exceed 12% with simple per annum interest (Section VI.B.) A change to simple interest, rather than compounding, is not the standard for current special district financing and could have myriad consequences on the ability of districts to finance public improvements.

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F.4: Suggested change: "The maximum net effective interest rate on any District Debt ~~**is not expected to**~~ **shall not** exceed twelve percent (12%)."
F.5: How are the following common financing terms affected by the simple interest requirement? (1) accreted interest and (2) capitalized interest. Underwriters will probably want clarity on this before structuring new debt.
F.6: Consider removing the term "proposed" from sentence "**proposed** maximum underwriting discount will be five percent (5%)."
G. Comments on Privately Placed Debt Limitation (Service Plan §V.A.10)
G.1: Definition should explicitly exclude loans from financial institutions registered with the Colorado Division of Banking. No benefit accrued to a District from obtaining an external certification of an interest rate on a loan issued by a "private" bank such as a credit union that is registered with the Colorado Division of banking. The true risk that should be mitigated by this section is non-financial institutions such as land developers loaning money to the district (usually controlled by the land developer) at 40%+ interest rates (i.e. Cundall Farms Metro, Amber Creek Metro, Lewis Pointe Metro, etc)
H. Comments on Debt Mill Levy (Service Plan §VI.B)
H.1: Recommend the base assessment rate remain at the 7.96% ratio to maintain consistency among districts throughout the City for the Gallagher adjustment.
H.2: Regarding change to allow mill levy adjustment to changes to the method of calculating assess valuation as of the **date of service plan approval**, rather than January 1, 2004: This adjustment is currently allowed for any changes occurring after January 1, 2004. The change to allowing this adjustment to changes occurring after the date of service plan approval will result in current special districts that have already been approved having a higher Maximum Debt Mill Levy than special districts approved under this new model service plan. This will provide a competitive disadvantage to the developments that have special districts approved under the proposed new model service plan.
H.3: Section VI.B. says "…other District obligations payable in whole or in part from revenues derived from the Debt Service Mill Levy..." "Debt Service Mill Levy" is not defined, the intent may have been to use "Maximum Debt Mill Levy".
I. Comments on O/M and Operating Mill Levy (Service Plan § VI.I) – See also Fee Limitations
I.1: Regarding expenses eligible to be paid with Operating Mill Levy, consider adding holiday lights. Those are huge with residential districts. What about social events often hosted by residential districts?
I.2: Regarding expenses eligible to be paid with Operating Mill Levy, add "retention" to "maintenance of **retention or** detention ponds.
I.3: Regarding ability to increase Operating Mill Levy higher than 10 mills, what happens if residents are not interested in serving on the Board? There are a lot of residential districts, even those which are fully built out and which have amenities, where it is impossible to get residents interested in serving on the Board. Is there any consideration for those instances other than a formal service plan amendment which is costly?

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I.4: Section I.C, change from:

"Ongoing operation and maintenance services are expected to be **repaid** by taxes imposed through a mill levy no higher than the Maximum Operating Mill Levy, and/or **repaid** by Fees as limited by Section V.A.18." to:

"Ongoing operation and maintenance services are expected to be **funded** by taxes imposed through a mill levy no higher than the Maximum Operating Mill Levy, and/or **funded** by Fees as limited by Section V.A.18."

I.5: Having flexibility on the imposition of an operations and maintenance mill levy is essential for several significant reasons, including, but not limited to, the following:

a) Metropolitan districts have specific operations and maintenance needs, the dollar amount for which will be determined as the development progresses, and for which a limited operations and maintenance mill levy would limit the Board from performing.

b) Typically, following organization, metropolitan districts conduct reserve studies for the operations and maintenance services to be provided by the metropolitan district in order for the metropolitan district to properly plan for those costs and determine the necessary operations and maintenance mill levy.

c) Having the ability to impose an operations and maintenance mill levy in an amount to fund the necessary operations and maintenance costs provides security that a metropolitan district's operations and maintenance needs can be addressed in a timely and cost-efficient manner.

d) Flexibility allows for the Board of a metropolitan district to determine if they wish to fund the operations and maintenance needs through the imposition of an operations and maintenance mill levy, through fees imposed by the metropolitan district, or a combination thereof.

e) It is essential that metropolitan districts have the ability to impose the necessary operations and maintenance mill levy to provide ongoing operations, maintenance, repair, and replacement of those public improvements for which the metropolitan district has responsibility. If the funds to operate and maintain these improvements are funded through an operations and maintenance mill levy the metropolitan district has security in knowing the funds will be received. If a homeowner fails to pay his/her taxes, a tax lien can be placed on the property and the tax lien will be sold ensuring the metropolitan district receives the revenue. This is not the case if a metropolitan district is limited in its operations and maintenance mill levy and must therefore heavily rely on fee revenue.

f) It is important that the property be maintained to the City's, the metropolitan district's, and other applicable entities/governance standards and that the Board of a metropolitan district is not restricted in the maintenance of the improvements.

g) The operations and maintenance mill levy is determined annually by the Board at a public hearing and a metropolitan district cannot impose a mill levy for the following year (i.e., 2021 mill levy for collection in 2022) in an amount that would exceed the revenue necessary to fund the budgeted operations and maintenance expenses, and any corresponding reserve fund, for that collection year.

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I.6: Limiting the operations and maintenance mill levy to 10.000 mills, as proposed under the revised Model Service Plan, will result in a metropolitan district not having adequate funding to operate and maintain public improvements. The proposed 10.000 mills will most likely only provide enough revenue to operate the basic statutory functions of a metropolitan district.

While the language in the proposed Model Service Plan allows for removal of the Maximum Operating Mill Levy restriction with City approval at such time as the Board is comprised of a resident majority, this process does not allow for full transparency of the property taxes and fees necessary to fund the operations and maintenance responsibilities and is contrary to the transparency and consumer protections that would be provided with disclosure of such information at the time of organization.

I.7: Metropolitan District Operating in Lieu of an HOA. As provided by state statute, it has become common for metropolitan districts to operate in lieu of homeowner associations (an "HOA"). Limiting the operating mill levy of a metropolitan district and, at the same time, limiting the ability of a metropolitan district to elect to supplement with the imposition of fees for operations and maintenance purposes essentially necessitates the need for an HOA in addition to a metropolitan district. This results in two governance structures both of which incur costs which are passed through to the residents resulting in increased costs to the residents. The multiple governance structure does not provide for the most efficient and transparent funding for such costs and services. In addition, the increased costs to the residents of having a multiple governance structure may impede development, especially of attached product, in the City.

There are many benefits to having a metropolitan district operate in lieu of an HOA, including, but not limited to, the following:

a) Cost Efficiency. Metropolitan districts fund their operations from revenues generated from real property taxes while HOAs assess dues and collect them from property owners. A metropolitan district can, therefore, operate more efficiently than an HOA as the collection of taxes is significantly more effective than separately billing individual homeowners, and dealing with the collection efforts.

b) Tax Deduction. In general, taxes paid to a metropolitan district are deductible from income taxes, while HOA dues are not.

c) Homeowner Savings. Out of pocket expenses for the residents are generally significantly less when paid through ad valorem tax as opposed to HOA dues. In addition, when a metropolitan district operates in lieu of an HOA, residents are not subject to two governance structures each of which incur costs payable by the residents.

d) Transparency. A metropolitan district is subject to various regulatory requirements that an HOA is not, such as:

   (i) All metropolitan district records must be made available to the public in conformance with the "Open Records Act", Section 24-72-201, C.R.S.;

   (ii) Public Meeting Laws as required by Section 24-6-402(2)(b), which require that all meetings of the Board of Directors at which public business is discussed or formal Board action may be taken must be open to the public;

   (iii) Code of Ethics applicable to all local governmental officials with additional standards imposed by Title 32, C.R.S. the ("Special District Act");

   (iv) The Taxpayer's Bill of Rights ("TABOR"), which prohibits metropolitan districts from incurring multiple fiscal year financial obligations without voter approval, and also imposes tax, debt, revenue, and spending limitations;

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(v) All metropolitan districts are subject to the Colorado Local Government Election Code and the Uniform Election Code of 1992; (vi) Metropolitan districts must have an audit, or an audit exemption, performed annually; and (vii) Metropolitan districts must file annual budgets, which budgets must be considered after the conduct of a noticed public hearing.
I.8: A district may not impose the Operating Mill Levy until the district has an Approved Conceptual Site Plan and a City IGA has been executed (Section VI.I.) • This change would hamstring the special district's ability to utilize the already limited Operating Mill Levy to cover some the general cost of operating the special district in the early stages of development and leads to the need for increased advances from the Developer which are then expected to be repaid with interest, thus, costing the special district more over time.
I.9: Regarding Maximum Operating Mill Levy of 10 mills restrictions: • The practical effect of this very limited Maximum Operating Mill Levy combined with the limitation of fees (discussed below), is that developments will have very limited amenities or will employ the use of HOAs (and their attendant fee authorizations) to cover the cost of the amenities that the special district cannot fund. The use of HOAs for this purpose causes a proliferation of entities that homeowners have to interface with which leads to increased homeowner confusion and frustration and creates administrative redundancies and inefficiencies in operating both a special district and an HOA, the cost of which is then bore by the homeowners.
I.10: Section V.A. says "The District shall not be authorized to operate and maintain any part of all the Public Improvements except as described in Section VI.I…" However, Section VI.I. does not discuss any authorization of the District to operate and maintain Public Improvements, only the District's authorization to impose the Operating Mill Levy. The only relevant language in Section VI.I. says, "the District will require operating funds for administration and to plan and cause the Public Improvements to be constructed and maintained."
J. Comments on Fee Limitations (Service Plan §V.A.18)
J.1: Must some or all Taxable Property in the District be owned or occupied by an End User before a District cannot impose and collect Fees?
J.2: Consider revising the sentence to place restriction on a lot-by-lot basis as follows: "The District may impose and collect Fees **on Taxable Property** as a source of revenue for repayment of Debt, capital costs, and/or for operations and maintenance until **such** Taxable Property is owned or occupied by an End User subsequent to the issuance of a Certificate of Occupancy for said Taxable Property."
J.3: The ability to impose penalties and charges is a necessary tool for Districts to ensure homeowner compliance, particularly when the District is functioning as an owner association. In addition, the ability to impose penalties or fines for delinquent payments of fees is a strong deterrent. We therefore recommend that the following language not be removed from VI.A and VI.E: "rates, tolls, penalties, or charges as provided in Section 32-1-1001(1), C.R.S., as amended from time to time"

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J.4: The most efficient and transparent method to fund the operations and maintenance costs of a metropolitan district is to have the flexibility to fund the majority, if not all, of the operations and maintenance costs through the imposition of property taxes (an operations and maintenance mill levy). If it is determined that additional funds are necessary to supplement the revenue received from the imposition of an operations and maintenance mill levy, it is essential that such fees be disclosed to prospective purchasers from the onset, with the understanding that such fees will need to adjust over time to take care of the finite improvements for which a metropolitan district is responsible to own, operate, and maintain. Limiting both the operations and maintenance mill levy as well as limiting the ability of a metropolitan district to impose fees for such purposes would have a devastating effect on the ability of a metropolitan district to perform the operations and maintenance services.
J.5: Section V.A.18 of the revised model service plan states: "No Fee related to funding operation and maintenance costs shall be imposed upon or collected from Taxable Property owned or occupied by an End User subsequent to the issuance of a Certificate of Occupancy for said Taxable Property unless and until the majority of the Board are Residents, and a majority of the Board has voted in favor of imposing and collecting Fees for the purpose of funding operation and maintenance costs of the District." Transparency for future and current homeowners and residents within a metropolitan district is paramount. Having the ability to determine the fees necessary, if any, to support the operations and maintenance needs of a metropolitan district from the onset is paramount.
J.6: Regarding O&M fees not to be imposed on an End User subsequent to a Certificate of Occupancy unless and until there is a majority resident-controlled board and the majority of the board has voted in favor of imposing fees (Section V.A.18) - See comment I.9 above regarding the interplay between the limitation of the Maximum Operating Mill Levy and the fees.
K. Comments on Disclosure Requirements (Service Plan §IX)
K.1: Per Section V.A. 18, Fees are limited to being imposed before the Residents and COs so is it necessary to require the Disclosure Notice to identify District Fees?
K.2: The disclosure form includes language that the "Mill Levy may fluctuate based on changes to residential rates. Despite the mill levy fluctuation, the amount of taxes paid by the homeowner should substantially stay the same from year to year." This statement is not accurate, as a District typically has the ability, subject to voter approval, to increase or decrease the O&M mill levy depending on financing needs, provided the O&M mill levy does not exceed the maximum O&M mill levy. As a result, homeowners may see the amount of taxes owed change not only as a result of changes to residential rates.
K.3: The Model Service Plan does not specify, though it is implied, whether the special district is responsible for ensuring that home buyers acknowledge the disclosures at time of contract. The concern with making this a responsibility of the special district is that the special district is not involved in the home buying/selling transaction and therefore cannot effectively comply with this requirement. Other jurisdictions have required that the special district provide the information to developers within the special district and/or post the information on its website; these requirements are more practical for the special district to comply with.

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L. Comments on Approved Conceptual Site Plan Requirement

L.1: In the summary of metro district changes, it states that City Council approval of a service plan amendment and an IGA required to identify debt and mill levy/fee authorizations once the CSP is approved. However, we do not see this language in the proposed model service plan. Will this proposed change be added to the proposed model service plan?

L.2: Regarding the proposed change to the city code that would require a Conceptual Site Plan be approved prior to the imposition of any mill levy or fees:

- In addition to the concerns noted above relative to the Operating Mill Levy, this would inhibit the ability of some special districts to issue early-stage debt and would force developers to find alternative funding sources. These alternative funding sources will undoubtedly be at a higher interest rate and ultimately have an adverse impact on the price of homes in the City. Perhaps a more sustainable alternative would be to require that the property need to be zoned prior to the imposition of any mill levy or fee. This would allow the bond market to determine the proper time to issue early state debt.

M. Miscellaneous Stakeholder Comments

M.1: Our comments are focused on the understanding that public improvements financed, owned, operated, and maintained by a metropolitan district are finite as they are only those public improvements identified in a corresponding Approved Conceptual Site Plan (as defined in the Model Service Plan), and not those that are to be owned, operated, and maintained by the City or other appropriate jurisdiction.

As such, upon identification of such metropolitan district responsibilities, the goal of a metropolitan district is to seek the most efficient and transparent method to finance the public improvements and to fund the related operation and maintenance costs.

M.2: We strongly encourage the City Council to consider the implications of the proposed changes to its regulations applicable to special districts and their impact on the future residential development within the City. We also hope that the Council will consider offering an opportunity for stakeholder engagement on this important issue before any final decisions are made.